

VZCZCXYZ0001  
RR RUEHWEB

DE RUEHKV #0760/01 1061324  
ZNY CCCCC ZZH  
R 151324Z APR 08  
FM AMEMBASSY KYIV  
TO RUEHC/SECSTATE WASHDC 5375  
INFO RUCNCIS/CIS COLLECTIVE  
RUEHZG/NATO EU COLLECTIVE  
RHEBAAA/DEPT OF ENERGY WASHINGTON DC

C O N F I D E N T I A L KYIV 000760

SIPDIS

SIPDIS

DOE FOR LEKIMOFF AND CCALIENDO

E.O. 12958: DECL: 04/08/2016

TAGS: [EPET](#) [ENRG](#) [PREL](#) [UP](#)

SUBJECT: UKRAINE: DAS BRYZA'S DISCUSSIONS ON ENERGY WITH  
PM TYMOSHENKO AND ENERGY MINISTER PRODAN

Classified By: THE AMBASSADOR, REASONS 1.4 B) AND D)

¶1. (C) Summary: In meetings April 4 with PM Tymoshenko and April 5 with Minister of Fuels and Energy Prodan, DAS Matt Bryza explored ways the USG could work with the GOU to bolster Ukraine's energy security. Tymoshenko said Ukraine needed to get direct access to central Asian gas, produce more domestically, and conserve gas at home. Bryza pointed out there might be options with supplies from Norway, with supplies from Azerbaijan and Turkmenistan more challenging. Both Tymoshenko and Prodan responded positively to the idea of Ukraine working together with Europe to get access to Central Asian gas. Both said in the ongoing gas negotiations Russia was insisting on retaining RosUkrEnergo as an intermediary. Prodan thought there also might be opportunities to work with the Europeans to displace RUE as a spot supplier to the European market, and also possibly work with them to increase pipeline capacity through Ukraine as a more economical option than Nordstream or South Stream. End Summary.

#### TYMOSHENKO'S VISION FOR ENERGY SECURITY

¶2. (C) DAS Bryza noted he was looking for strategies that would help Ukraine to stand with the Europeans and channel Gazprom toward market-based behavior. Tymoshenko agreed that energy independence was essential, and that Ukraine in the past had opportunities to bolster independence but its leadership had proven weak and irresolute. Now, she said, the problem is much more difficult than when she was Deputy PM for energy in 2000.

¶3. (C) Tymoshenko outlined her strategy. On gas, Ukraine first had to restore direct links with Turkmenistan. She saw no reason why Turkmenistan could not sell directly to Ukraine and the EU. Secondly, Ukraine needed to access better its own deposits of gas. This meant attracting international investors, and her government's current review of Production Sharing Agreement laws was designed to assist this. Finally, Ukraine needed to reduce gas consumption, and in some areas it could substitute other fuels for gas. As a last option, they could take Russia to Stockholm arbitration for violating the 2004 agreement, but this would be a difficult option, she said. For nuclear fuels, she felt Ukraine needed to produce more elements of the nuclear fuel cycle domestically, with the exception of enrichment. For oil, Ukraine had access to oil transiting the Black Sea, but needed to utilize the Odesa-Brody pipeline and possibly build a new refinery in central Ukraine to process Caspian crude and increase the pipeline's offtake.

SOURCES OF GAS

14. (C) Bryza thanked Tymoshenko for outlining a strategy that in many ways reflects our own. He noted Europe has three major potential sources of gas. Azerbaijan (with possibly some gas from Iraq) could supply the Turkey-Greece-Italy and Nabucco pipelines. Even though this gas would not directly go to Ukraine, it could help stabilize prices in Europe by providing competition to Gazprom. Norway was adding 44 BCM by 2013 and there was the potential to move some of this via Denmark and Poland to Ukraine. Then there was Turkmenistan, but it was difficult to get President Berdymukhammedov to be courageous and think of supplying the West. Bryza noted the Azeris had told us there had recently been some feelers from Ashgabat about connecting Turkmenistan's Block 1 deposit with Azerbaijan's transport infrastructure, which is only 60 kilometers away. Bryza made similar points to Prodan.

#### JOINT ACTION WITH EU ON GAS ACCESS TO CENTRAL ASIA

15. (C) With both Tymoshenko and Prodan, Bryza noted there also could be possibilities to move Azeri or Turkmen gas via White Stream or LNG, though these options faced political and commercial challenges. Another option could be to secure delivery of Turkmen and Kazakh gas via Russia's pipeline system, if the Ukrainians and Europeans could act together to demand such third-party access, perhaps in a commercial venture involving the EU and its international financial institutions. Both responded very positively to this idea. Tymoshenko said if they could set up a long-term gas arrangement with Turkmenistan, the transport could be worked out, with White Stream her preferred option, although she would be willing to look at LNG if that was more economical than a pipeline. She stated she had spoken during the recent visit to both President Bush and Secretary Rice about direct access to Central Asia and found them supportive. Bryza noted that Gazprom was relying on Central Asian gas to

fulfill its European supply contracts, and that the Shtokman (in the Barents Sea) and Bovanenkov (on Russia's Yamal Peninsula) were years behind schedule and would be unable to feed Nordstream or South Stream for at least 10 years. Tymoshenko was adamant that Gazprom would not secure ownership or control of Ukraine's gas storage or transit pipelines, adding Ukraine had passed a law under PM Yanukovich that specifically prohibited any transfer.

#### TOUGH GAS TALKS

17. (C) Both Tymoshenko and Prodan indicated gas talks with Russia were very tough. Prodan said the Russians were offering the simple choice of accepting RosUkrEnergo's (RUE) continuing and murky role as an intermediary or immediately pay USD 315/thousand cubic meters, with no explanation why. Tymoshenko also related that their signals from the negotiators were that Russia was clinging to RUE. She insisted it was essential to eliminate RUE and other shady intermediaries, and said it would be helpful if Ukraine were to get some public support. Bryza suggested the U.S. could offer such support; but he also stressed the need for Ukraine to demonstrate its reliability as a gas transit country.

#### TAKING THE "JUICY BUSINESS" FROM RUE

18. (C) Prodan saw another way the EU might be able to cooperate with Ukraine. Currently, Ukraine's contract with RUE obligated it to offer gas transit and storage to RUE at bargain rates. RUE paid Ukraine USD 7.80 for storage, when in Europe the going rate was closer to USD 30, he said. The contract also mandated Ukraine to offer RUE storage at this price for up to 10 bcm for 20 years. RUE used this gas to sell cheaper Central Asian gas on European spot markets, earning massive profits. As one of Prodan's aides remarked, it was curious why Gazprom would cede this particularly "juicy business" to RUE. Prodan suggested that there was no reason the Europeans, perhaps through a consortium, could not take over this business. They could buy the gas at the Russia/Ukraine border, could store it in Ukraine's gas storage, and then use it themselves to meet spot needs, thus avoiding paying RUE's spot prices. Bryza agreed this might

be interesting, and would also help increase transparency between the EU and Ukraine on gas matters.

#### INCREASING GAS CAPACITY IN UKRAINE

¶9. (C) Prodan noted that in the first quarter of 2008, Ukraine had transported a record amount of gas to Europe. He remarked that it was thus ironic that the Europeans continued to believe the Russians' line that Ukraine was a unreliable gas transit state. He added that since 2004 Ukraine and Russia had a project to expand the Ukrainian system's capacity by 19 bcm with a parallel pipeline to eliminate a bottleneck across the Carpathians from Bohorodchany to Uzhgorod. This project, which only would cost USD 800 million, would be practically free compared with Nordstream and South Stream. Now, however, the Russians he said were silent about this project. Bryza said we might talk to the Europeans about this -- perhaps they could step in and help move this forward. (Bryza will forward to the interagency community a paper outlining this proposal, which also includes the elements outlined in para. 8.)

¶10. (U) Note: DAS Bryza cleared this message.

Taylor